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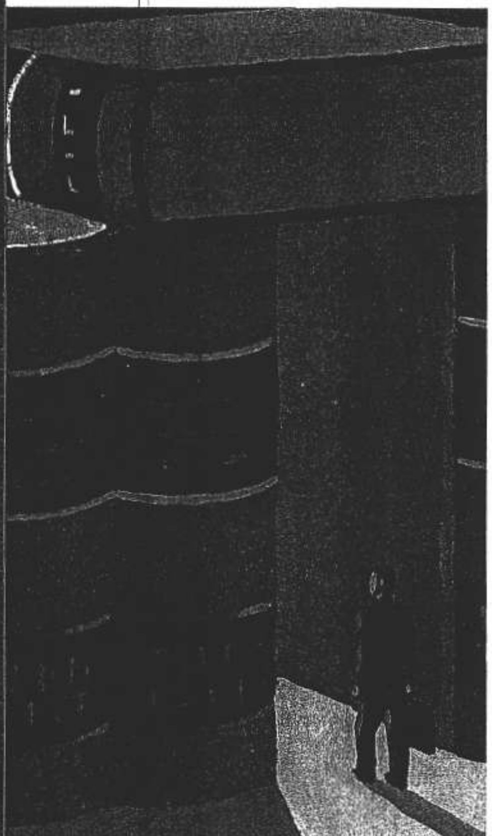

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Coevolving: At Last, A Way to Make Synergies Work

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Coevolving

At Last, a Way to Make Synergies Work

KATHLEEN M. EISENHARDT AND
D. CHARLES GALUNIC

Executive Summary

THE PROMISE OF SYNERGY is the prime rationale for the existence of the multibusiness corporation. Yet for most corporations, the 1+1=3 arithmetic of cross-business synergies doesn't add up.

Companies that do achieve synergistic success use a corporate strategic process called *coevolving*; they routinely change the web of collaborative links among businesses to exploit fresh opportunities for synergies and drop deteriorating ones. The term *coevolution* originated in biology. It refers to the way two or more ecologically interdependent species become intertwined over time. As these species adapt to their environment, they also adapt to one another.

Today's multibusiness companies need to take their cue from biology to survive: They should assume that links among businesses are temporary and that the num-

ber of connections–not just their content–matters. Rather than plan collaborative strategy from the top, as traditional companies do, corporate executives in coevolving companies should simply set the context and then let collaboration (and competition) emerge from business units.

Incentives, too, are different than they are in traditional companies. Coevolving companies reward business units for individual performance, not for collaboration. So collaboration occurs only when two business-unit managers both believe that a link makes sense for their respective businesses, not because collaboration per se is useful. Managers in coevolving companies also need to recognize the importance of business systems that support the process: frequent data-focused meetings among business-unit leaders, external metrics to gauge individual business performance, and incentives that favor self-interest.

CAPTURING CROSS-BUSINESS SYNERGIES is at the heart of corporate strategy—indeed, the promise of synergy is a prime rationale for the existence of the multibusiness corporation. Yet synergies are notoriously challenging to capture. Shell's initial attempt to launch a common credit card across Europe failed. Allegis, United Airlines' bid to build synergies in related travel businesses like hotels and airlines, was dismantled. Amazon.com has yet to see significant synergies from its PlanetAll acquisition, which was supposed to drive additional sales by linking to people's Rolodex of family and friends. The truth is, for most corporations, the 1+1=3 arithmetic of cross-business synergies does not add up.

So how do the companies that actually achieve synergies do it? Their managers have mastered a corporate strategic process called *coevolving*. These managers routinely change the web of collaborative links—everything from information exchanges to shared assets to multibusiness strategies—among businesses. The result is a shifting web of relationships that exploits fresh opportunities for synergies and drops deteriorating ones. (See "Disney versus Sony: Contrasting Cases in Patching and Coevolution" at the end of this article.)

The term *coevolution* originated in biology. It refers to successive changes among two or more ecologically interdependent but unique species such that their evolutionary trajectories become intertwined over time. As these species adapt to their environment, they also adapt to one another. The result is an ecosystem of partially interdependent species that adapt together. This interdependence is often symbiotic (each species helps the other), but it can also be commensalist (one species uses the other). Competitive interdependence can emerge as well: one species may drive out the other, or both species may evolve into distinct, noncompetitive niches. Interdependence can change, too, such as when external factors like the climate or geology shift.

A classic example of symbiotic coevolution is the acacia tree and the *pseudomyrmex* ant species. Ants need acacias for nectar and shelter. Acacias depend on the ants stinging to protect them from herbivores. Over time, the acacia has evolved to make it easy for the ants to hollow out thorns for shelter and to have access to its flowers. Similarly, the ants have evolved into a shape that makes it easier to enter the acacia flower. Together, the species are better off than they would be if they didn't collaborate.

Scholars from many disciplines have recognized that biological coevolution is just one kind of complex adaptive system. Recently, computer simulations have uncovered general laws of how these systems work, including social systems such as multicountry economies and multibusiness corporations. These laws reveal nonlinear effects such as leverage points with disproportionate impact on the entire system. They show how the number of connections can affect the agility of a system. And they indicate that complex adaptive systems are most effective when intelligence is decentralized. More generally, these laws are consistent with the notion that multibusiness corporations are coevolving ecosystems.

So what does all that mean for today's multibusiness companies? In essence, they need to take their cue from nature and approach cross-business synergies with a very different mind-set. Managers at coevolving companies assume that links among businesses are temporary. They think "Velcro organization." They also recognize that the number of connections—not just their content—matters. So they manage the tension between fewer links for agility and more links for efficiency. While traditional corporate managers plan collaborative strategy from the top, corporate executives in coevolving companies don't try to control or even predict it. They set the context and then let collaboration (and competition) emerge from business units. Incentives are different, too. Coevolving companies reward business units for individual performance, not for collaboration. Thus, collaboration occurs only when two business-unit managers both believe that a link makes sense for their respective businesses, not because collaboration per se is useful. Finally, managers in coevolving companies recognize the importance of business systems: frequent data-focused meetings among business-unit leaders, external metrics to gauge individual business performance, and incentives that favor self-interest. (See the table "Traditional Collaboration Versus Coevolution.")

Coevolving is a particularly crucial strategic process in new-economy corporations, where higher-velocity markets drive managers to keep individual businesses small enough to adapt but intense competition demands that they maintain economies of scope and rapid cross-business learning. Not surprisingly, many leading corpo-

Traditional Collaboration vs. Coevolution

	Traditional Collaboration	Coevolution
Form of collaboration	Frozen links among static businesses	Shifting webs among evolving businesses
Objectives	Efficiency and economies of scope	Growth, agility, and economies of scope
Internal dynamics	Collaborate	Collaborate and compete
Focus	Content of collaboration	Content and number of collaborative links
Corporate role	Drive collaboration	Set collaborative context
Business role	Execute collaboration	Drive and execute collaboration
Incentive	Varied	Self-interest, based on individual business-unit performance
Business metrics	Performance against budget, the preceding year, or sister-business performance	Performance against competitors in growth, share, and profits

rations with significant Internet businesses like Sun, Schwab, and Hewlett-Packard coevolve. Since even pre-IPO companies in the new economy often have multiple businesses, very young firms like eye-care specialist NovaMed coevolve as well. And finally, coevolving is crucial for knowledge-intensive corporations like consultancy Booz-Allen & Hamilton and product design firm IDEO, which constantly share learning throughout their organizations.

Our ideas about coevolving developed from a decade of research into successful corporate strategy in intensely competitive, fast-moving industries. Coevolution in natural ecosystems, we found, looks a lot like the collaborative webs within corporations that achieve significant multibusiness synergies. And both of these resemble the external ecosystems that link corporations together in webs of alliances. More generally, the disciplines of biology and complexity yield important insights into how superior corporate strategy—inside and outside the corporation—happens in dynamic markets.

Shift Collaborative Webs

In traditional corporations, the web of collaborations among businesses often freezes into fixed patterns. Business units share intangible resources such as brands, physical resources such as manufacturing facilities, or organizational capabilities such as product development. Once the patterns are established, they're not revisited regularly. By contrast, managers in coevolving corporations frequently reconnect the links among businesses. Some links last a long time, others are much shorter. And while some links lead to predicted synergies, others open up unanticipated ones.

GE Capital is an example of a company that reconnects its collaborative webs. GE Capital was launched with collaborative links to GE's consumer businesses, such as refrigerators and dishwashers. As time went on, GE Capital gained enough scale and expertise to offer its financing services to GE's more sophisticated industrial products businesses like power plants and jet engines. The collaborative web shifted more toward these areas. The combination of products and innovative financing fed the growth of both GE Capital and the industrial products businesses. Eventually, GE Capital became its own web of interconnected businesses, like specialty insurance and credit card operations, by developing common acquisition procedures and sharing customers. As a result of that changing collaborative web, GE managers created synergistic growth beyond what static collaborations could have achieved.

Another company we'll call OfficeSys provides a detailed illustration of the types of collaborations that managers at coevolving companies use. Three years ago, OfficeSys was dominated by two large businesses: photocopiers and fax machines. For many years, those businesses had shared optical technologies and product components. As industry price cutting slashed margins, the managers of the two businesses combined their manufacturing and procurement activities. As a result, both were able to cut costs and compete more effectively in their markets. At about the same time in 1997, corporate executives at OfficeSys launched two new businesses around a revolutionary optical scanning technology that captures data for transfer to the Internet. These managers collaborated very informally by trading engineers back and forth in order to share scarce and costly talent. They also collaborated on developing a software protocol standard for data transmission among different Internet-connected devices.

But as is often the case in coevolving companies, the collaborative web evolved. When the two new businesses began to ship products, their managers ended the informal swapping of engineers. The managers of the fax business joined the software standard collaboration. The managers of all four businesses now have a joint advertising campaign to promote their collective brand.

The OfficeSys example is striking because of the variety of collaborations that took place. Some collaborations were major and long term, such as the joint development of common product components. Some were modest and transient, like the informal trading of engineers. Some were focused on creating revenue, like the software protocol initiative and brand building. Some drove down costs, like shared manufacturing. And they occurred all along the value chain, from R&D to marketing. Because of their coevolutionary efforts, OfficeSys's managers strengthened their businesses in the maturing photocopier and fax markets and grew their businesses in the emerging Internet appliances markets.

What drives managers to reconnect their collaborative webs? Sometimes it's changes in the market, pure and simple. For example, increased cost pressures forced managers at OfficeSys to expand manufacturing links between their mature businesses. Sometimes it's changes in the business units themselves. Managers pursue new directions, adjust to the changing business roles of sister divisions, or simply grow their businesses. Most commonly, it's a combination of the two.

NovaMed Eyecare Management, a fast-growing, successful health-care company, is an example of how changes made by an individual business unit can reverberate throughout the larger business group, affecting how other units relate to one another and how they all relate to the market. In 1995, NovaMed's eye-care medical practices throughout the United States were similar. The collaborative relationships among the practices focused on saving costs through common information systems, bulk purchasing, and shared staff.

The doctors in one practice, however, had particularly strong research skills, especially in refractive surgery. They decided to put those skills to use. As the doctors became the innovators and new laser technology for eye surgery was approved by the FDA, the pattern of collaboration shifted. Sharing resources to lower costs was still important, but the transmission of surgical innovations became far more crucial. That is, doctors at the research-driven practice pioneered new surgical procedures and then broadcast them throughout NovaMed.

In 1998, NovaMed launched a new kind of business, one that conducted clinical trials of surgical equipment and their related procedures for medical device companies. The doctors at the research-based practice worked closely with this new business, which strengthened their ability to pioneer leading-edge surgical techniques. Some of the more research-oriented doctors within the other practices also began collaborating with the clinical trials business. As a result, NovaMed was able to build the critical mass of participating doctors and patients necessary for meaningful clinical trials. Not surprisingly, the company has grown over 60% during the first half of 1999 compared with 1998, and it went through a successful IPO. More to the point, NovaMed's practices have moved much faster and with greater

In coevolving companies, e-businesses compete with their bricks-and-mortar counterparts and new technologies compete with established ones.

medical skill than competitors into refractive surgery, one of the hottest growth segments in health care.

Bring the Market Inside

Managers at companies that follow the traditional rules for collaboration avoid internal competition on the grounds that it devastates teamwork, wastes resources, and cannibalizes existing products and businesses. By contrast, managers at coevolving companies let collaboration and competition coexist. E-businesses compete with their bricks-and-mortar counterparts, new technologies compete with established ones, and so on. While senior managers don't actively seek out competition, they don't discourage it if it occurs naturally as the result of alternative technologies, business models, distribution channels, and the like. Just as the distinction between friend and foe is blurring in the alliance webs outside the corporation, it is also blurring on the inside.

An exemplar of such thinking is Hewlett-Packard. For decades, the tension between competition and cooperation has helped HP thrive. A classic example involves the desk- and laser-jet printing technologies. Eventually the two businesses evolved into different market niches and became enormous businesses in their own right, but for several years they competed for the same customers. The company's managers knew they could not predict how the market would unfold, so they let the two compete until it became clear whether one would dominate or whether the businesses would diverge into viable market niches. Had the managers at HP squelched this competition by choosing one technology over the other, they would have lost out on a collective $15 billion business opportunity. Recently, that same kind of competition has emerged between HP's UNIX and NT computing businesses. Initially, UNIX was the primary business. Then NT looked to be the winner. Now with the rise of Linux and repeated NT delays, UNIX is resurgent. The result of such competition is that HP can win regardless of how the market unfolds.

Letting internal competition flourish is particularly important in the Internet world. Managers who think in terms of coevolution let Net businesses compete with established ones. A good example is Siebel Systems, a "best of breed" provider of enterprise software for sales and marketing. Siebel's managers didn't let the usual concerns about channel conflict keep them from quickly entering e-commerce. In fact, Siebel's new subsidiary, Sales.com, initially targeted the same customers as the existing business—major global corporations with complex selling requirements. Early on, the two diverged; Sales.com sold Web-hosted application products directly to individual salespeople in these corporations, and the traditional business concentrated on selling software for the entire sales force to senior executives. Sales.com's products turned out to be most appealing to small and mid-sized companies that found Web-hosting to be an attractive alternative to enterprise software resident on their own IT equipment. By letting competition unfold, Siebel managers figured out how to play the Internet game well before other ERP companies like PeopleSoft, while keeping their established business successful.

Balance the Number of Links

Traditional corporations focus on picking the right collaborations. By contrast, coevolving companies recognize that the *number* of collaborative ties is often just as significant as the kinds of collaborations. They balance the tension between too many links that restrict adaptation and too few that miss important opportunities for synergies.

A terrific example is Vail Ski Resorts. When the group formed in a 1997 merger, the rationale was to gain extensive synergies by tightly linking the four member resorts—Vail, Breckenridge, Keystone, and Beaver Creek—with numerous collaborations, particularly branding under the Vail name. It was a classic, top-down plan to create synergies—with the usual sub-par results. Vacationers wanted unique resort experiences, not four "would-be Vail" destinations. Once senior managers cut back on these connections, they could more freely adapt their resorts to their evolving markets. For example, Breckenridge's location next to a classic mining town has particular appeal for European skiers seeking a "Western" experience. Breckenridge's managers capitalized on this attraction by introducing unique features that appeal to these skiers, such as longer-stay vacation packages. Loosening the connections also allowed Vail Resorts' managers to figure out, over time, the right number of connections among the resorts. Today the resort group collaborates—by choice—in only a few high-payoff areas: supplies procurement, integrated information systems, and interchangeable lift ticketing.

When markets become dynamic and agility matters most, businesses need fewer collaborative connections.

As a general rule, more links among businesses make sense when markets are stable. In such circumstances, economies of scope dominate. Disney's approach to the Internet illustrates this principle. In general, Disney's businesses are highly connected. But the company's managers intentionally entered the volatile Internet world with businesses that were only weakly tied together. Their Infoseek business, in fact, was not even fully owned. Figuring that the old business models might not make sense, managers wanted plenty of freedom to evolve in and even shape whatever the emerging market spaces would be. They understood that agility—not control—matters in fast-moving markets. Yet now that the Internet markets are more crystallized, Disney's managers have aggressively linked their Internet plays with one another and other parts of Disney. Once again, economies of scope drive Disney's thinking. They bought the rest of Infoseek, combined it with other Internet businesses such as Disney Travel Online into a single business (Go.com), made their content Web sites accessible from a single portal (Go Network), and created new links to established businesses like ESPN. Of course, the jury is still out on whether they connected too soon in the volatile I-world.

By contrast, when markets become dynamic and agility matters most, businesses need fewer connections in order to adapt. Consider the British Broadcasting Company. For years, the radio station, television broadcast, and television production businesses were tightly linked, even to the point of cross-subsidization. Radio, in particular, was viewed as the decidedly unglamorous cash cow. But, in one of the surprises of the Internet, radio's prospects have changed. Why? Many people shut off their televisions and turn on their radios for background entertainment while they surf the Web. So BBC has loosened the links among its businesses to let radio evolve more freely in the higher-velocity, less predictable Internet space.

Uncover the High-Leverage Links

Especially in fast-paced markets, managers don't have time to oversee a lot of collaborative initiatives. So it's crucial to figure out what links are sensible, identify the high-payoff ones, and forget the rest. Typically, the highest-payoff links can be leverage points with disproportionate synergies.

A great example is the U.S. multichain retailer Dayton Hudson. There are only a few collaborative links between the rapidly growing Target chain and upscale retailers Marshall Field's and Dayton's. But senior managers have located a simple link that gives them a lot of leverage: regular exchange of fashion information. Target, in particular, has benefited. Its managers learn about fashion trends much sooner than competitors by paying attention to the upscale retailers, whose buyers spot trends early through their contacts with leading fashion designers. (For example, Target got wind of the recent "gray craze" from other Dayton Hudson managers and tailored its apparel and home furnishings accordingly.) This link helped Target managers to reposition the chain as "hip fashion at a low price" and achieve double-digit sales and profit growth that buried competitors like Kmart and J.C. Penney. So does this success mean that Target should add more links? Absolutely not. In fact, for Target, more links such as common buyers might actually slow the retailer down, raise costs, and lower the synergistic value of the businesses. In other words, fewer links—targeted at the right content—can, counterintuitively, create more synergies.

The exact location of these high-leverage links depends upon a company's resources, the relatedness of its businesses, and its strategic position. Take Cisco and

Ascend, two competing stars of the turbulent networking industry. Given the pace and uncertainty of that industry, it makes sense for managers at both companies to focus on just a few collaborative areas. But because their circumstances are different, their managers have chosen different links. Cisco has a huge market cap, which makes acquisitions relatively affordable. Managers have used that advantage brilliantly: they have developed a shared acquisition process—from target identification through due diligence to integration—that capitalizes on learning-curve effects of acquisitions throughout the corporation. Managers use this shared process to make frequent acquisitions that supplement in-house R&D and open up new product areas. In effect, Cisco's managers transfer R&D risk to venture capitalists and then scoop up the winners. Ascend, in comparison, was launched well after Cisco. When the company was young, its managers couldn't afford acquisitions to open up new product areas. But they needed to move very fast with a low profile to stay well ahead of Cisco. So Ascend's managers concentrated their cross-business collaborations on aggressively sharing software and other product components across businesses. This collaborative link preserved precious financial resources, accelerated time to market and, at least initially, kept Ascend off Cisco's radar screen.

The most effective decision makers are those at the business-unit level, where strategic perspective meets operating savvy.

Lay the Foundation

Understanding the essentials—frequently reconnect the relationships among businesses, blur collaboration and competition, manage the number of connections, and uncover high-leverage links—is crucial for companies that hope to coevolve. But it's not enough. There is an underlying foundation of structures and processes that managers must build if coevolution is to work.

LET BUSINESS UNITS RULE

A cornerstone of that foundation is letting heads of business units determine where and when to collaborate. If corporate managers take the lead, they often do not understand the nuances of the businesses. They naively see synergies that aren't there. They tend to overestimate the benefits of collaboration and underestimate its costs. Conversely, if junior managers take the lead, they lack the strategic perspective to pick the best opportunities. They may spot good opportunities for collaboration, but they rarely uncover the best ones. Thus, the most effective decision makers are those at the business-unit level, where strategic perspective meets operating savvy.

The locus of decision making at General Electric is a prime example. General managers of GE's businesses have regular meetings to search for cross-business synergies. These meetings typically include managers from related businesses where synergies could be expected. They engage in what is called "receiver-based communication." That is, they share information about their activities, and interested managers from other businesses (the "receivers") follow up as they see appropriate. Even though senior executives may suggest areas of collaboration and individual business managers are expected to attend the meetings, nobody is forced to collaborate. Business general managers make the collaborative calls.

That doesn't mean that corporate-level managers have no role in cross-business collaboration. On the contrary, senior executives create the context in which that collaboration can happen. They act as "pollinators" of ideas as they travel among businesses. They stage modern-day bazaars that bring business-level managers together to talk and to perhaps find collaborative opportunities. They determine the lineup of businesses within the corporation by patching businesses against market opportunities so that effective collaboration can emerge. They ensure that each business is strong enough to be an attractive partner. They also foster a culture of information sharing by assigning synergy managers within individual business units. These executives may even suggest particular collaborations for individual businesses. But they don't force collaboration. (For more on the executive roles, see "Patching, Coevolving, and the New Corporate Strategy" at the end of this article.)

BUILD THE MULTIBUSINESS TEAM

Another cornerstone of coevolution is the multibusiness team—the group of business unit heads that orchestrates collaborations among their businesses. The key to making these teams work well is frequent group meetings. In the most successful coevolving companies, these meetings happen at least monthly and are "don't miss" events. The content of these meetings is a run-through of real-time internal operating numbers and external market statistics, as well as a qualitative discussion of shared interests such as competitors' moves, customer feedback, and technology developments. The meetings are fact-focused and pragmatic. Often managers discuss a specific strategic issue facing one or more of the businesses. Since travel can be a problem, effective teams rely a lot on videoconferences. They add fun to the mix, too. Eli Lilly's managers, for example, organize some meetings in enticing locations like London, where they give executives time to shop, visit local pubs, or sightsee.

The most obvious effect of frequent meetings is that business heads become acquainted with opportunities for collaboration. But just as important, they weave the social fabric of familiarity and trust that supports effective collaboration. (See "The Power of Multibusiness Teams" at the end of this article.)

Consider Time Warner. Its managers are notoriously uncollaborative, and compared with other media giants, the corporation as a whole has not gained much synergistic value from its businesses. However, managers from the Turner Sports group, *Sports Illustrated* magazine, and the sports wing of HBO started meeting often. As a result, they have learned about one another's needs and resources. These meetings have led to several collaborative efforts, including the Turner Games boxing events. These were organized by Turner Sports, promoted and broadcast on HBO, and covered by *Sports Illustrated*.

A more subtle, albeit well-known, effect of these meetings is the emergence of roles. For example, at Vail Ski Resorts, their weekly meetings helped managers shape the business roles of their own ski areas in relation to one another. Vail's role, for example, has become the "capital of skiing," while Breckenridge evolved into the "Western" experience. Establishing very clear turf boundaries helped the managers of those businesses communicate more clearly and collaborate more effectively by lowering political tension and clarifying opportunities. The result is that Vail Ski Resorts competes very successfully against competitors like Intrawest because of its distinctly focused ski experiences and effective synergies.

Finally, frequent meetings can lead to the emergence of a shared intuition. As managers regularly review the operating performances and markets of all the businesses together, they develop a common understanding—a gut sense—of the patterns shaping their industry. Because these meetings focus managers on factual data, their shared intuition remains tightly linked with shifting realities and helps multibusiness teams identify the best collaborations quickly.

But in certain situations (notably related businesses facing a small number of competitors), that shared intuition can deepen into a multibusiness strategy that goes beyond particular business roles to include coordinated pricing, technology and product road maps, and customer segmentation. This happened at a global computing company we'll call Cruising. The managers of Cruising's primary computing businesses instituted bimonthly meetings to track their turbulent industry. Over time, the different businesses developed distinct roles and a shared multibusiness strategy. For example, one business was in the fastest-growing, highest-margin segment of the industry. So it became the golden goose, and the company's overall strategy was to protect and grow this business. A second business took on the workhorse role. It was the largest business and sold the greatest number of products, so it contributed manufacturing volume and routines for many basic business processes. It also relayed information about low-end competitors attacking the golden goose from below. A third business competed in a small, high-margin segment of the industry. That business helped several other Cruising businesses to gain sales by promising delivery of these short-supply, high-quality products if the customer bought other products from Cruising. As a result of this multibusiness strategy, Cruising became the industry's company to beat.

GET THE INCENTIVES RIGHT

If coevolving requires multibusiness teams that can quickly identify and execute collaborative opportunities, then the incentives for business-unit heads must reward collaboration. Right? Wrong. Business-unit managers who coevolve their businesses are rewarded for self-interest, *not* for collaboration. That is, they are rewarded primarily for their individual business performance. That performance is measured externally against key competitors—not internally against planned, preceding year, or sister-business performance—with the metrics typically being a mix of growth, profit, and market share. The ultimate reward, as in professional sports, is being on the team. So, for example, the manager of a business in a very competitive market does not need to post the same numbers as a manager who competes with better strategic position. Both are expected to excel in their own markets. If they do, they are on the team and are well compensated. If not, they're off.

Rewarding self-interest works because it's simple. It turns the attention of business-unit managers to the most important thing they need to do—win in their own markets. By contrast, mixed incentives (some group, some individual) confuse and demotivate people. Self-interest works for another reason, too. It makes market realities, not friendship, the basis of collaboration. In particular, it banishes the "good people collaborate and bad people don't" thinking that leads to ineffective collaboration. Finally, rewarding self-interest works because win-win collaborations usually create the biggest synergistic pie for the corporation, even when individual businesses get unequal slices. It's true that occasionally an opportunity that's great for the corporation is missed because it was not so good for the businesses—but in dynamic markets, worrying about the corporate optimum is just too slow.

Individual-based incentives run counter to the culture of companies that place a high value on collective behavior. But these companies pay a price. Take Mitsubishi. Mitsubishi outwardly has some of the infrastructure of coevolving companies, such as regular Friday lunch meetings for business-unit heads. The collectivist culture at Mitsubishi, however, has led to some ineffective collaborations. For example, *keiretsu* members purchased steel inside Mitsubishi even though better deals were available from outside suppliers. Similarly, fellow keiretsu member Kirin protected its premium beer business from internal competition and subsequently lost to outsider Asahi in key growth segments of the Japanese beer market.

Of course, even in the best coevolving companies, collaborative efforts may not happen when they should. Rather than switch to rewarding collaboration, coevolving executives look for alternatives: they improve information flow so that managers can see collaborative opportunities better; repatch closely aligned businesses together into larger business segments; or repair businesses that others may be avoiding because they are ineffective. What coevolving managers *don't* do is reward collaboration.

Is Coevolving Right for Your Company?

Capturing cross-business synergies is an essential part of corporate strategy. Yet many managers collaborate in too many areas or for too long, or they focus on the wrong opportunities. They forget that, especially in high-velocity markets, there's not a lot of time to collaborate. They neglect to update their collaborative links as businesses and markets emerge, grow, split, and combine. Of course, some managers simply ignore cross-business synergies, an approach that often beats poor collaboration. But it also defeats the point of the multibusiness corporation. Coevolving is a better alternative.

Coevolving is a subtle strategic process. In fact, it's a bit counterintuitive—build collaborative teams and yet reward self-interest, let competition flourish, don't worry too much about efficiency, collaborate less to gain more. Coevolving turns the corporation into an ecosystem with corporate strategy in the hands of business-unit managers. But it is precisely this oblique thinking that gives coevolving companies a competitive edge.

Disney Versus Sony: Contrasting Cases in Patching and Coevolution

IN THE MID-1990s, Sony scored a box-office hit with *Men in Black*, while Disney had a similar box-office success with *The Lion King*. *Men in Black* grossed more money in its first weekend than almost any other film in history. For Sony, the $600 million box-office and video revenues were much of its success story. For Disney, those revenue sources were just the opening chapter. Disney's managers also released more than 150 kinds of *Lion King* merchandise (pencil cases, dolls, T-shirts, and so forth), turned the soundtrack into a musical sequel called *Rhythm of the Pride Lands*, and produced a video entitled *Simba's Pride*. The total take was approximately $3 billion. Disney also introduced *Lion King* themes at existing resorts and ultimately at its new Animal Kingdom theme park.

Most people understand the 1+1=3 arithmetic of Disney's collaboration, which funnels the same content into multiple media businesses. But few people recognize that Disney's managers use different collaborative patterns with different products. *Beauty and the Beast* became a play on Broadway, for example, whereas *Toy Story* was turned into a video game, and *The Little Mermaid* became a television show. Even fewer people understand that Disney's managers engage in many kinds of collaborative efforts that change over time. Managers of Disney World and the Big Red Boat cruise line collaborate on joint vacation packages to boost revenues for both businesses, for example. EuroDisney executives share knowledge about hotel management and ticket pricing with other resort managers. ESPN managers work with the Internet businesses to share sports content and with the theme parks to launch ESPN restaurants. Touchstone Studios occasionally shares actors with animated films. Thus, Disney's managers have effectively patched together a changing quilt of entertainment businesses like theme parks, movie studios, retail stores, and broadcast networks. Simultaneously, they have created the corporate context (like synergy managers in each business, corporate Imagineers, and the Disney Dimensions program) that permits the coevolving mix of collaboration among these businesses. (For more on how Disney creates synergies, see "Common Sense and Conflict: An Interview with Disney's Michael Eisner," in HBR January–February 2000.)

By contrast, Sony's managers have not patched businesses such as theme parks, publishing, and retail outlets into their company, even though other entertainment companies have found that they're important for creating corporate synergies. They also have some businesses that on the surface seem synergistic but aren't. For example, Sony's Walkman products obviously depend on media content, but consumers are unlikely to listen to Sony-produced music just because they have a Walkman. Further, Sony's managers have been less effective in capturing the collaborative opportunities they do have because of long-distance relationships between business heads in Tokyo and New York. Not surprisingly, then, Disney has outperformed Sony in many one-on-one matchups like *The Lion King* versus *Men in Black*—and more generally in the creation of corporate value in the entertainment industry.

The Power of Multibusiness Teams

IN TRADITIONAL CORPORATE STRATEGY, the multibusiness team—the group of business-unit managers that oversees synergies among businesses—simply doesn't exist. And yet, it is an organizational requirement for coevolutionary companies. The team's primary job is to orchestrate the shifting collaborative web among the businesses. Most of the time, these managers represent their own businesses. But we have also observed that business-unit heads often temporarily assume functional perspectives. Those who have experience in engineering or marketing, for example, take on those perspectives, especially when the team is discussing multibusiness strategy. Members also take on other, equally distinctive roles—devil's advocate, conservative, innovator, to name a few—which can further enhance the team's effectiveness.

The multibusiness team is powerful because it can add significant value to the corporation beyond the sum of the businesses. Without the teams, individual business managers have difficulty finding collaborative links, developing the social relationships with other business heads that facilitate collaboration, and even conceptualizing a collective strategy. The multibusiness team can also create corporate value that the market cannot duplicate with a portfolio of investments. The market cannot reproduce either the deep understanding of collaborative possibilities that can exist among team members or the underlying social structure that enables effective collaborations over time. Of course, especially in very dynamic markets, many of the best collaborative links are outside the corporation. But even then, the market holds no advantage when multibusiness teams work well together and yet also focus on achieving individual business success.

The key to superior multibusiness teams is great group dynamics: fast decision making with plenty of conflict over content, but also with deep social bonds that limit interpersonal conflict. To create this group process, these teams rely on frequent meetings to build familiarity and trust, data-rich information to develop a shared intuition, and clear turf boundaries so that politicking is kept to a minimum.

Patching, Coevolving, and the New Corporate Strategy

TRADITIONAL CORPORATE STRATEGY CENTERS on establishing defensible strategic positions by setting corporate scope, acquiring or building assets, and weaving synergies among them. The result is sustained competitive advantage. Yet in high-velocity markets, strategic position can quickly erode. In these markets, the strategic *processes* by which managers reconfigure resources to build new strategic positions are more pivotal to corporate performance than any particular strategic position. The new corporate strategy focuses on these freshly defined corporate strategic processes.

One of these processes is patching. Patching is the frequent remapping of businesses to fit changing market opportunities. It involves combining, splitting, exiting, and transferring businesses within the corporation. (For more on the concept of patching, see Kathleen M. Eisenhardt and Shona L. Brown, "Patching: Restitching Business Portfolios in Dynamic Markets," HBR May–June 1999.) A second is coevolving.

With patching, corporate executives set the lineup of businesses within the corporation and keep it aligned with shifting markets. Their key skill is recognizing changing patterns in product and customer segments and in technology road maps. With coevolving, multibusiness teams (the heads of individual businesses working together) drive synergies by reconnecting the collaborative links among businesses as markets and businesses evolve. Their key skill is managing their own group dynamics.

While patching and coevolving are distinct corporate strategic processes, the two are often intertwined. For example, NovaMed's coevolution from purely cost-oriented collaboration among its different medical practices to innovation-oriented collaboration was enhanced when a new clinical-trials business was patched into the company. The new business strengthened the payoff from innovation-based synergies.

Seven Steps to Kick-Start Coevolution

1. Begin by establishing at least monthly, must-attend meetings among business heads that enable them to get to know one another and to see collaborative opportunities.
2. Keep the conversation focused on real-time information about operating basics to build intuition and business roles. Include one or two specific strategic issues within or across businesses.
3. Get rid of "good people collaborate, bad people don't" thinking by rewarding self-interested pursuit of individual business performance against rivals.
4. When collaborative opportunities arise, remember that many managers get stuck on their first idea. Instead, brainstorm to expand the range of possible collaborative tools—from simple information sharing to shared assets to strategy—and collaborative points along the value chain.

5. Realistically analyze the costs and benefits of the most promising options. Remember that benefits usually appear greater than they are.
6. Fine-tune as you go. Up-front analysis is never a substitute for real-time learning.
7. Avoid "collaboration creep." Take the time to cut stale links.

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